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SUBJECT: Brazil: Morgan Stanley's Dismal View of 2009 Growth
Prospects: Outlier or Leading Indicator?

REF: Sao Paulo 216

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¶1. (SBU) Summary: Economic growth in Brazil will fall to negative 4.5 percent this year, Morgan Stanley country manager Daniel Goldberg told Ambassador Sobel in an April 23 meeting. Goldberg cited low corporate confidence and weak industrial production numbers as the main drivers. His firm expects unemployment rates to jump, creating negative spillovers into other sectors. Although Morgan Stanley is definitely an outlier in its dismal economic forecast, the firm's pessimistic analysis does point to trends that could potentially deepen the crisis in Brazil. The financial community's consensus GDP growth estimate, however, is for an economic contraction of approximately 0.5 percent. End Summary.

Morgan Stanley Pessimistic on Brazil 2009 Growth

¶2. (SBU) Morgan Stanley country manager Daniel Goldberg told the Ambassador that if growth in Brazil were to remain flat for the rest of the year, the economy would contract by 1.5 percent for 2009 overall. According to Morgan Stanley, Brazil's economy contracted in the fourth quarter of 2008 at an annualized pace of 13.6 percent, the worst quarter in the country's history. (Note: The quarterly growth rate was negative 3.6 percent. End Note.) Morgan Stanley predicts a 1.8 percent negative growth rate for the first quarter (based on preliminary data), negative 1.6 percent for the second, and zero growth for quarters three and four. These numbers form the basis of their overall annual negative 4.5 percent prediction.

The Gap Between Consumer and Corporate Confidence

¶3. (SBU) For Goldberg, the gap between consumer confidence and corporate confidence indicates the likely direction of the Brazilian economy. Although consumer confidence remains relatively high (despite a decline since the crisis; see reftel)--98.5 points out of a possible 200, with 100 being average--he believes the lack of corporate confidence--now at 77.9 points--will eventually translate into massive layoffs, pushing unemployment to 12 percent or even higher. (Note: March unemployment reached nine percent. End Note.) As unemployment increases, Goldberg says this "meltdown"

will lead to a massive economic contraction. He maintains that once consumer confidence dips to numbers in line with corporate confidence, the economy could experience a deeper recession than Morgan Stanley's official prediction.

14. (SBU) In further support for their pessimistic forecast, Marcel Carvalho, Morgan Stanley's Executive Director for Research, published a paper citing a study from the Getulio Vargas Foundation (FGV) that stated that 18.5 percent of firms judge their inventories to be too high. He maintained that inventory contractions were largely responsible for last quarter's massive decline. Carvalho anticipates that firms will continue to reduce inventories, resulting in further production cuts and more layoffs.

Morgan Stanley: Outlier or Leading Indicator?

15. (SBU) Comment: Among financial institutions, Morgan Stanley has by far the most pessimistic prediction for economic growth in Brazil. Most other banks have taken a more optimistic view, most recently citing numbers as high as zero percent growth for 2009 (Reftel), though it is important to note that over the last four months there have been consistent downward revisions of these growth forecasts. Economic data continue to show a mixed bag, with recent retail sales numbers showing an increase of 3.8 percent (reflecting Goldberg's view that most consumers do not believe the crisis has or will seriously affect them), industrial capacity operating at 77.7 percent (a low rate not seen since 1993), and a moderating labor market with layoffs actually decreasing (though job creation is still weak). Taken together, the data support weak economic conditions in Brazil, though most financial analysts would argue

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that Brazil is well-positioned to confront the financial crisis. While Morgan Stanley's prediction of negative 4.5 percent growth is by far the most pessimistic opinion (three percentage points below the next lowest prediction and 4.1 points below the consensus average of all financial institutions), the consensus analyst forecast of slight negative growth (about half a percentage point) is more realistic than the Finance Ministry forecast of two percent growth. End Comment.

16. (U) This cable was coordinated with and cleared by Embassy Brasilia and the Financial Attache in Sao Paulo.

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